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Revenue Procedure 87-54

Rev. Proc. 87-54; 1987-2 C.B. 669; 1987 IRB LEXIS 94; 1987-41 I.R.B. 37

July 1987

[*1]

APPLICABLE SECTIONS:

26 CFR 601.602: Forms and instructions

TEXT:

SECTION 1. PURPOSE

The purpose of this revenue procedure is to provide procedural guidelines to exclude certain prizes and awards granted after December 31, 1986, from gross income under *section 74 (b) of the Internal Revenue Code*. As amended by *section 122 of the Tax Reform Act of 1986* (the Act), 1986-3 (Vol. 1) C.B. 26, *section 74 (b)* provides that if certain prizes or awards are transferred by payers to governmental units or charitable organizations described in *section 170 (c) (1)* or *(2)* of the Code, respectively, pursuant to "designations" made by recipients, the prizes or awards are not included in the recipients' gross income.

This revenue procedure describes a safe harbor that ensures that such prizes or awards qualify for the exclusion. However, other designation methods meeting the requirements imposed by *section 74 (b) of the Code* may also be used.

SEC. 2. BACKGROUND

.01 *Section 74 (a) of the Code* provides, in general, that gross income includes amounts received as prizes and awards. Taxable prize and award amounts of \$600 or more paid in any taxable year by a payer to a recipient that are not paid for services rendered are to be reported [*2] by the payer on Form 1099-MISC, Statement for Recipients of Miscellaneous Income. See *section 6041 (a) of the Code* and *section 1.6041-1 (d) (3) of the Income Tax Regulations*.

.02 *Section 74 (b) of the Code*, an exception to the general rule of *section 74 (a)*, provides that gross income does not include amounts received as prizes and awards made primarily in recognition of religious, charitable, scientific, educational, artistic, literary, or civic achievement, but only if (1) the recipient is selected without any action on the recipient's part to enter the contest or proceeding, (2) the recipient is not required to render substantial future services as a condition to receiving the prize or award, and (3) the prize or award is transferred by the payor to a governmental unit or a charitable organization described in paragraph (1) or (2) of *section 170 (c)* pursuant to a designation made by the recipient.

The third requirement of *section 74 (b)* was added by *section 122 of the Act*, effective for prizes and awards granted after December 31, 1986.

.03 S. Rep. No. 9-313, 99th Cong. 2d Sess. 50 (1986), 1986-3 (Vol. 3) C.B. 50, states:

Under the bill, the present-law exclusion under *section 74 (b)* [*3] for certain prizes and awards for charitable, artistic, scientific, and like achievements is modified to apply only if the recipient designates that the prize or award is to be transferred by the payer to a governmental unit or a tax-exempt charitable, educational, religious, etc. organization contributions to which are deductible under *section 170 (c) (1)* or *170 (c) (2)*, respectively, if such designation is made and the prize or award is so transferred to a governmental unit or charitable organization by the payor, the prize or award is not included in the winner's gross income, and no charitable deduction is allowed either to the winner or to the payor on account of the transfer to the governmental unit or charitable organization.

For purposes of determining whether a prize or award that is so transferred qualifies as excludable under the bill, the present-law rules concerning the scope of *section 74 (b)* are retained without change. In addition, in order to qualify for the *section 74 (b)* exclusion as modified by the bill, the designation must be made by the taxpayer, and must be carried out by the organization making the prize or award, before the taxpayer uses the item that is awarded [*4] (e.g., in the case of an award of money, before the taxpayer spends, deposits, invests, or otherwise uses the money). Disqualifying uses by the taxpayer include such uses of the property with the permission of the taxpayer or by one associated with the taxpayer (e.g., a member of the taxpayer's family).

SEC. 3. DESIGNATION GUIDELINES

.01 If the taxpayer wishes to exclude from gross income a prize or award (or portion thereof) that meets the requirements of *section 74 (b) (1)* and (2) of the Code, the taxpayer must make a designation pursuant to which the prize or award is to be transferred to an organization or entity described in *section 170 (c) (1)* or (2). This "designation" should be made before the prize or award is actually presented by the payor to the recipient to avoid the possibility of a disqualifying use of the prize or award by the recipient.

.02 The designation preferably should be made by the recipient on a form provided by the payor and returned to the payor. However, the recipient may make an effective designation in a written document prepared by the recipient and submitted to the payor. In either case, the designation should (1) describe the purpose of the document by [*5] reference to *section 74 (b) (3) of the Code* and (2) indicate the designee governmental unit(s) or charitable organization(s). The designation may also state the federal income tax consequences or making the designation.

Language for a model designation document follows below:

The purpose of this document is to designate pursuant to *section 74 (b) (3) of the Internal Revenue Code* the governmental unit(s) or charitable organization(s) described in *section 170 (c) (1)* or (2) of the Code, respectively, to which a prize or an award amount (or portion thereof) is to be transferred.

The undersigned recipient of the (describe nature and total value of prize or award) awarded (or to be awarded) on (date) requests that the payor, (name and address), of this prize or award transfer it, in the amount(s) indicated, to the entity (entities) designated below:

Amount	Designee
	to (Name and Address of sec-

tion 170 (c) (1)
or (2) entity)

(List separately each designee if
more than one)

to Section 170
(c) (1) or (2) en-
tity or entities to
be selected by
the payor.

The undersigned recipient understands that the amount(s) of the prize or award designated above is (are) excludable from the recipient's gross income [*6] under *section 74 (b) of the Code* but is (are) not deductible by the recipient as a charitable contribution.

Recipient's signature (or signature of authorized representative)

Recipient's Taxpayer Identification Number

Recipient's address

Date signed

.03 If it is not possible for the recipient of a prize or an award to make a designation prior to the actual receipt of the prize or award, as in the case of an unexpected presentation, the recipient must, before the item is used, return the prize or award to the payor and should make a designation in the manner set forth in section 3.02 above, with an additional paragraph stating: "The undersigned certifies that no use of this prize or award was made prior to its return to the payor."

.04 If the recipient makes a designation pursuant to section 3.02 or .03, the payor should provide a written acknowledgment to the recipient stating when and to whom the designated amounts were transferred by the payor. The acknowledgment should incorporate language substantially as follows:

To: (name, taxpayer identification number, and address of recipient)

In accordance with your directions, the property, to the extent designated, (state nature and value thereof), [*7] representing the (name of prize or award) granted to you was transferred to (name of *section 170 (c) (1) or (2) organization(s)*) on (date).

Signature of payor or authorized representative (state title)

Payor's taxpayer identification number

Payor's address

Date signed

.05 The designation and acknowledgment documents (or copies thereof) should be retained by both the payor and the recipient of the prize or award. These documents will be accepted by the Internal Revenue Service as evidence that

the requirements of *section 74 (b) (3) of the Code* have been met.

SEC. 4. EFFECTIVE DATE

This revenue procedure applies to prizes and awards granted after December 31, 1986.